IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO **DIVISION OF FINANCIAL MANAGEMENT** **APRIL 2005 VOLUME XXVII NO. 10**

Submitted for your contemplation and edification, we present a dichotomy. Did you know Idaho has the distinction of being both one of the first states to enact a sales tax and one of the last states to enact a sales tax? This is not a trick question or some belated April Fool's Day gag. It really is true. Let us explain.

It is a little known fact that Idaho actually enacted its first sales tax in 1935. At that time, the Legislature feared Idaho would lose federal funding for relief programs related to the Great Depression if it did not contribute to relief efforts. In an attempt to assure federal relief funds would continue flowing into the Gem State, "The Co-operative Emergency Revenue Act of 1935" was passed by the Idaho Legislature during the First Extraordinary Session of 1935. Governor C. Ben Ross signed it into law on March 20, 1935, earning the sales tax the nickname "pennies for Bennie."

According to the ACIR (U.S. Advisory Commission on Intergovernmental Relations, Significant Features of Fiscal Federalism, February 1993) only fifteen states had enacted a sales tax earlier – Mississippi in 1930; Arizona, California, Illinois, Iowa, Michigan, New Mexico, North Carolina, Oklahoma, South Dakota, Utah, Washington, and West Virginia in 1933; and Missouri and Ohio in 1934.

Interestingly, as enacted, the 2% Idaho sales tax was designed to last just two years, from March 15, 1935 to March 15, 1937. However, it never made it to its second birthday. Soon after the sales tax passed, signatures began being collected to put it to a vote of the citizens of Idaho. They voted down the sales tax in the 1936 General Election. It appears the people of Idaho felt even two years were too long for the sales tax to be around.

Three decades would pass before Idaho would have a sales tax again. Nearly 30 years to the day the first sales tax was approved, on March 24, 1965, Idaho Governor Robert E. Smylie signed into law a 3% sales tax. By doing so, Idaho again joined the ranks of states with sales taxes. However, unlike its predecessor, this version of the sales tax was permanent.

Only six other states have enacted sales taxes after Idaho – Massachusetts, New Jersey, and Virginia in 1966, Minnesota and Nebraska in 1967, and Vermont in 1969. Of course, there are five states (Alaska, Delaware, New Hampshire, Montana, and Oregon) that currently have no sales tax.

Within our neighborhood (i.e., six surrounding states) Idaho is definitely "middle-of-the-road" as far as the sales tax rate is concerned. Two neighboring states (Oregon and Montana) do not have a sales tax. Utah and Wyoming both have state rates that are lower than Idaho's (4.75% and 4%, respectively). Washington and Nevada both have higher state sales tax rates of 6.5%.

Another often-overlooked aspect of Idaho's sales tax is that we have very minimal "local option" sales taxes in Idaho. According to the Sales Tax Clearinghouse, when the combined state and local levies (averaged for the entire state) are examined, Idaho's 5.05% comes in at the low end of the spectrum by a wide margin. Closest to Idaho is Wyoming at 5.25%, followed by Utah at 6.4%, then Nevada kicks the combined rate up to 7.15%. Washington tops the list (and is in fact third highest in the nation) at a whopping 8.25% combined state and local sales tax rate – on average.

Idaho's sales tax rate is scheduled to drop from 6% to 5% on July 1, 2005 after spending 26 months at the higher rate. The timing of this rate reduction was put in place in 2003 as part of the legislation that increased the rate temporarily in order to meet Idaho's critical spending needs. Changing the state's sales tax rate to meet spending needs is not unprecedented. For example, one of the first actions of the 1983 Legislature was to temporarily raise the sales tax rate from 3% to 4%. However, even before it had adjourned, the Legislature raised the rate again from 4% to 4.5%. During the next legislative session, a 4% permanent sales tax rate was adopted. This rate remained in place until April 1986 when it was temporarily raised to 5%. This rate was made permanent the next year.

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General Fund Update

As of March 31, 2005

	$ Millions		
Revenue Source	FY05 Executive Estimate[3]	DFM Predicted to Date	Actual Accrued to Date
Individual Income tax	974.5	669.4	662.4
Corporate Income tax	120.6	66.7	80.3
Sales Tax	933.4	701.0	711.8
Product Taxes[1]	22.4	16.8	17.1
Miscellaneous	105.9	55.5	64.4
TOTAL GENERAL FUND[2]	**2,156.9**	**1,509.5**	**1,536.0**

1 Product Taxes include beer, wine, liquor, tobacco and cigarette taxes
2 May not total due to rounding
3 Revised Estimate as of January 2005

March was a very good month for General Fund revenue, with all components coming in at or above expectations. For the month the excess was $21.4 million, bringing the fiscal year-to-date excess to $26.5 million. The greatest strength was in the individual income tax, with $12.5 million more than expected in March. Corporate income tax collections and sales tax collections were each ahead by $4.0 and $4.1 million, respectively.

Individual income tax collections were $12.5 million higher than expected in March, and are $7.1 million BELOW expectations for the year to date. This year-to-date shortfall is a function of refund timing (significant acceleration that is not reflected in the historical data), and is expected to reverse itself by fiscal year-end. In fact, the reversal appears to have already begun as March refunds were $4 million LOWER than expected based on historical timing patterns. Withholding payments in March were $2.2 million higher than expected, and filing payments were $5.9 million higher than expected for the month.

Corporate income tax revenue was $4.0 million higher than expected in March, and is $13.6 million higher than expected for the year to date. This revenue category is relatively small, less than 6% of total General Fund revenue in FY 2005. However, the forecasted growth rate for this year is 20.3% adjusted for law changes, 17.1% after allowing for the effect of law changes. Actual March growth (over March 2004) was 77%, and the actual year-to-date growth rate as of the end of March is 59%. March's corporate strength is due to refunds that were $0.4 million (52%) lower than expected, miscellaneous diversions that were $1.6 million (75%) lower than expected, and estimated payments that were $1.8 million (36%) higher than expected.

Sales tax revenue was $4.1 million (6.3%) higher than expected in March. Actual growth for March (over March last year) was 12.5%. The current executive forecast for the full fiscal year is for 7.8% growth adjusted for law changes, 5.3% after allowing for the effect of law changes. Actual year-to-date growth in the sales tax is 8.3%. This is exactly 3 percentage points stronger than expected for the full year.

Product taxes were exactly on target in March, and miscellaneous revenues were $0.8 million ahead of expectations on strength in the Insurance Premium tax and interest earnings, partially offset by weakness in unclaimed property.